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C O N F I D E N T I A L SECTION 01 OF 03 HARARE 000970

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AF/S FOR H.SERVIN-BAEZ  
SENIOR AFRICA DIRECTOR C. COURVILLE  
STATE PASS TO USAID FOR M. COPSON AND E.LOKEN  
TREASURY FOR J. RALYEA AND B. CUSHMAN  
COMMERCE FOR B. ERKUL

E.O. 12958: DECL: 08/01/2015  
TAGS: [ASEC](#) [ECON](#) [PGOV](#) [PHUM](#) [PREL](#) [ZI](#)  
SUBJECT: GONO ANNOUNCES MONETARY STATEMENT BOMBSHELL

Classified By: Charge d'affaires Michael Raynor under Section 1.4 b/d

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Summary  
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¶1. (C) In his mid-term Monetary Policy Statement on July 31, Reserve Bank Governor Gideon Gono announced a currency redenomination that will slash three zeros from Zimbabwe's inflation-ridden notes. This conversion will be carried out through August 21, after which the old notes will become worthless. In addition to the redenomination, the Governor also repeated his earlier announcement that an entirely new currency would be introduced at an undisclosed date and that this conversion would take less than a week. Gono announced a 60-percent devaluation against the US dollar and the formation of an ill-defined exchange rate review board that would adjust the rate in the future. Although Gono granted some relief to exporters and bankers, his statement and Finance Minister Herbert Murerwa's fiscal statement the week before offer mere bandages to Zimbabwe's deepening economic crisis. End Summary.

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Slashing Three Zeros in 21 Days  
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¶2. (SBU) Amidst a slew of catchy slogans, Gono stated that beginning on August 1 a new series of bearer checks would begin to replace the old bearer checks, resulting in the deletion of three zeros from the currency. For instance, the Z\$100,000 bearer check will be replaced with a new Z\$100 bearer check. Correspondingly, retail prices are supposed to be adjusted also by deleting three zeros. At a diplomatic briefing after the statement, Gono admitted that cutting the

zeros will not improve the situation on its own, but he justified the move as a convenience to the country's accountants and data storage systems. This conversion is to occur through August 21, after which the old bearer checks will become "garden manure" in Gono's words.

13. (SBU) Gono justified the conversion as an attack against speculative trading in goods and foreign exchange, which he blamed for fueling inflation. Accordingly, he announced limits on the amount of old bearer checks that can be converted into the new checks ) Z\$100 million for individuals and Z\$5 billion for companies. Anything in excess would require certification from a government agency that the money was obtained legally. Gono stated that police, revenue collectors, and "very enthusiastic jobless youth" would be deployed to border posts and airports to prevent traders from returning more than the allowed Z\$5 million in currency held abroad. Since the statement, police have assembled numerous roadblocks in and around Harare and have asked to search even diplomatic vehicles looking for large amounts of currency. Police have been seen confiscating amounts deemed by the officers to be &excessive8.

14. (SBU) Reiterating his last monetary statement in January, Gono again promised that a new currency was planned but did not state when it would be revealed. He however warned that the conversion to the new currency would be swift, taking not more than seven days after the announcement. Gono even suggested to the diplomats that this conversion might take as little as 24 hours.

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A Token Devaluation, Promise of Further Review  
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15. (SBU) Gono declared an immediate 60-percent devaluation of the local currency from Z\$101,195:US\$ to Z\$250,000:US\$. (N.B. The parallel rate is about Z\$600,000:US\$.) He also stated that an Exchange Rate Impact Assessment Board, comprised of government, exporters, importers, and the Consumer Council, had been created to periodically review the exchange rate. The devaluation and the creation of the exchange rate board were not included in the printed version of Gono's speech, suggesting to us that this was the most contentious point of the statement and was agreed to only at the last minute.

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Gono Delivers Modest Relief  
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16. (SBU) Gono's statement offered some reprieve to key sectors of the economy. He did away with the prior requirement that exporters remit unused balances in their foreign currency accounts (FCAs) to the Reserve Bank after 30 days. Aiming to combat gold smuggling, Gono also increased the percentage of hard currency earnings that gold exporters can keep in their FCAs. For tobacco growers, he introduced a new price support and stated that as of next April tobacco exporters would be allowed to retain 15 percent of their hard currency earnings in FCAs. Gono also provided a sizable cushion to the embattled banking sector by loosening liquidity controls and reducing the Reserve Bank's accommodation window rate by 550 percentage points to 300 percent for secured capital. Gono also relaxed new minimum capital requirements that were set to be introduced later this year.

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Statement Sends Traders and Consumers Spinning  
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17. (SBU) The announced redenomination has sparked general

confusion among businesses and consumers as they struggle to determine what it means for their prices and cash holdings. Consumers in Harare greeted the announcement with a buying spree as they raced to spend money that will expire in three weeks and buy durable goods that will retain their value. Some retailers in Harare closed shop the afternoon of the statement as the merchants tried to determine how to price their goods. In a move likely to spread, one Harare school has asked parents to pay now for the school term that begins in September, so that the school can quickly buy hard currency as a cushion against this uncertainty.

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Fiscal Review - Weak Productivity, Ballooning Deficit  
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¶8. (SBU) Preceding Gono's statement, Finance Minister Herbert Murerwa on July 27 delivered the Mid-Term Fiscal Policy Review and supplemental budget request. Murerwa grasped at a few illusions of economic recovery - unrealistic estimates of maize and wheat production, and an uptick in tourist arrival driven primarily by cross-border traders. Overall, however, he painted a dire picture of the state of the nation's finances and recited a litany of underperformance by sector: poor tobacco production, a further 10 percent decline in mining, a depressed manufacturing sector, and poor performance and weak

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governance among most parastatals.

¶9. (SBU) Murerwa offered little indication of a return to fiscal probity any time soon. Zimbabwe's domestic debt has tripled since December 2005, in large part due to the failure of loss-making parastatals to service their debt and their call on government to take over the obligations. Public external debt as of 30 June 2006 amounted to US\$3,968 million while arrears came to US\$2,122 million.

¶10. (SBU) Murerwa conceded that soaring inflation had not only spurred the rate of revenue collection over the past half year, but had also driven up expenditures. Accordingly, he shifted upward the tax brackets ) although he failed to match inflation. Murerwa also trumpeted new sources of revenue such as new toll roads, and proposed higher taxes and import duties on some items. These measures, however, would fall well short of expenditure commitments.

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Comment  
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¶11. (C) Once again, the GOZ has embraced cosmetic economic gestures at the expense of fundamental economic reform. While Gono's monetary policy statement offers minor reprieve to some sectors, it does not address the underlying causes of inflation, and will likely generate massive confusion. Although Gono noted that the redenomination was modeled after a similar exercise in Mozambique, the economic policies in the two countries are night and day, and it is only a matter of time before hyperinflation reinstates the three zeros on the Zimbabwean dollar. Mozambique is also converting the currency over six months whereas Zimbabwe has only 13 banking days to carry it out.

¶12. (C) The speed at which the GOZ is executing the conversion suggests to us that it intends to catch many Zimbabwean dollar holders ) both in the country and abroad ) unaware, effectively stealing their money by decree. Against all this uncertainty, the parallel exchange rate is certain to spike as worried cash holders scramble for safe haven. A day after Gono's monetary statement, Harare residents are nervous and, recalling the monetary statement last year that preceded Operation Restore Order, fearful that this latest statement foreshadows a black market crackdown.

RAYNOR